R4105-80A

The Conference Board

Volume 2, Number 7 July / August 1991

Economic Times

INSIDE:

- **Industry Outlook Report**
  (special center section)
- **A Challenge to the Professional Pessimists**
  (pages 4-5)
- **Why is Immigration Like the 1947 Dodgers?**
  (pages 6-7)
- **Colloquium Looks at Health Insurance**
  (page 3)
- **Stat File and Crystal Ball**
  (pages 8-11)

Editor's Note

This month we again offer our quarterly round-up on the outlook for various industries — see the shaded center section — prepared by specialists in each of the industries.

On the following page our special Colloquium panel on health care tells us what needs to be done about the many Americans who lack adequate insurance.

Next, we get a historical rundown on the parallel paths through the centuries taken by progress and pessimism. And then Julian Simon analyzes the often overlooked benefits of immigration.

See you all next in September. Meanwhile, have a good summer.

Ed Fiedler

Maxim of the Month

In forecasting, give 'em a number or give 'em a date, but never both.

Attributed to Sir Alec Cairncross

Anemic? Or Vigorous? Yes!

With most analysts now agreeing that the 1990-91 recession has ended, forecasters have turned their attention to the vigor of the recovery. That debate is more interesting than most — analytically somewhat richer than usual, and for once it seems the arguments are, except (as usual) for the yellow-dog business journals, being conducted in a more gracious manner.

There are persuasive arguments on both sides. The consensus forecast calls for a growth rate of about 3 percent from mid-'91 to mid-'92. Only a few hardy optimists are projecting a cyclical recovery equal to the 6-percent historical norm — the average pace of recovery following the eight recessions since World War II.

But the optimists make some strong arguments. Perhaps the best is history, the fact that during the first 18-24 months almost every cyclical recovery since World War II has recorded a growth rate in the neighborhood of 6 percent. In addition, there are at least three important sectors of the economy with good credentials for a strong rebound: First, consumption, where the surveys of expectations have rebounded very encouragingly; second, exports, where the depressed international exchange value of the dollar — yes, still low, even after the run-up this spring — puts U.S. producers at a substantial competitive advantage in world markets (see Stat File comments, p.8, and chart, p.10); and third, inventories, which despite being kept under good control before the downturn have been liquidated heavily during the recession, suggesting the need for some very substantial re-stocking during the recovery.

Those who forecast a slower recovery make a good case, too. They note, first, that the demographics are a lot less favorable than a decade ago — 1.4 million new households are expected to be formed this year, in contrast to 1.9 million in the early 1980s. Second, real interest rates on bonds and other long-maturity borrowings remain high, dampening the outlook for housing, heavy construction and other interest-sensitive activities. Third, contrary to the usual practice, federal taxes have not been cut and federal spending has not been boosted to help stimulate the recovery.

Fourth, the 1990-91 recession was a mild one, and past experience tells us that mild recessions tend to beget milder than average recoveries. Finally, and perhaps most important, there is the fact that most of the history from which the 6 percent average recovery is calculated was recorded back when the underlying productivity trend was pushing 3 percent per year, rather than the 1 percent rate that has characterized the past two decades. What this suggests is that before we use the historical average as a norm we probably ought to reduce it by a couple of percentage points. If we don't, a "normal" recovery is going to exceed the economic speed limit and, after a year or so, generate a new upsurge of inflationary pressures. Which, no thank you, we very much do not need.

Who's going to win this argument? How vigorous will this recovery prove to be? My guess is still that it'll be stronger than consensus but short of the historical norm. But let's not forget the only honest answer to that question: **Nobody knows!**

Copyright 1991 by The Conference Board.
Economic Times (ISSN 1050-0200) is published 10 times annually (July/August and November/December are combined issues) by The Conference Board, Inc., 845 Third Avenue, New York, N.Y. 10022-6601. Printed in Alpha, New Jersey. Second-class postage paid at New York, N.Y. and other mailing offices. POSTMASTER: Send address changes to *Economic Times*, 845 Third Avenue, New York, N.Y. 10022-6601. Editor: Edgar R. Fiedler

The Conference Board, 845 Third Avenue, New York, New York, 10022
The Conference Board Europe, Avenue Louise, 207 - Bte 5, B-1050 Brussels, Belgium
The Conference Board of Canada, 255 Smyth Road, Ottawa, Ontario, KIH-8M7

Colloquium: Health Care Insurance

Background:

Although most Americans receive competent health care the costs of which are covered by health insurance, about 33 million of us live without that basic security, and tens of millions more are inadequately covered. Further, anecdotal evidence suggests that for many families insurance is becoming very difficult to obtain even at much higher prices.

Question:

What should be done to make health insurance available to those not now covered?

Henry J. Aaron
The Brookings Institution

All methods of achieving universal financial access to health care have serious flaws. The "worst system except for all the others" and therefore the best is to make employment-based insurance mandatory and extend public coverage beyond medicare and Medicaid to everyone not connected to families with a member in the labor force. Major alternatives, such as immediate adoption of national health insurance or tax-credit based schemes, involve enormous institutional disruption and income redistribution.

John T. Dunlop
Harvard University

Initially a specified basic benefit package is required, followed by access steps phased with tough cost constraints. First, reform the insurance market for small business to preclude selecting-out high risks. Second, provide tax credits to small business. Third, eliminate state mandates of insurance beyond a basic package. Fourth (later), federalize Medicaid with a buy-in for the unemployed. Fifth (eventually), require purchase or provision of a basic benefit package from regional funds administered by private insurers selected competitively.

Walter J. McNerney
Northwestern University

Given federal budget targets and the lack of enthusiasm among voters to spend more, we will have to settle for incremental steps. A place to start would be to mandate a minimum benefit package for most employers, with provision for tax breaks for small employers. Also, we should institute a federal/state program focused on the mother and child. To ignore such steps much longer will leave our credibility as a humane society in serious doubt throughout the world.

Victor R. Fuchs
Stanford University

Universal coverage requires two things. First, the government must use compulsion for those unwilling to obtain insurance voluntarily (i.e., gamblers and "free riders"). Second, the federal government should use general revenues to substitute premiums for the poor and for the non-poor who face abnormally high premiums because of bad health. Existing patterns of insurance distribution should be tried first. If they prove to be unsatisfactory, government-sponsored national health insurance would be necessary.

Members:

Members of The Conference Board Economics Colloquium are: Stephen H. Axilrod, Vice Chairman, Nikko Securities International; Andrew F. Brimmer, President, Brimmer & Company; Don R. Conlan, President, Capital Strategy Research; Robert G. Dederick, Executive Vice President and Chief Economist, Northern Trust Company; John T. Dunlop, Lamont University Professor Emeritus, Harvard University; Lyle E. Gramley, Senior Staff Vice President & Chief Economist, Mortgage Bankers Association; Isabel V. Sawhill, Senior Fellow, The Urban Institute; Charles L. Schultze, Senior Fellow, The Brookings Institution; James Tobin, Sterling Professor Emeritus, Yale University; Laura D'Andrea Tyson, Professor of Economics, University of California, Berkeley; Charls E. Walker, Chairman, Charls E. Walker Associates; Murray Weidenbaum, Director, Center for the Study of American Business; Albert M. Wojnilower, Senior Advisor, First Boston Corporation. For this special topic we have added Henry Aaron, Director, Economic Studies Program, The Brookings Institution; Victor Fuchs, Henry J. Kaiser, Jr. Professor, Stanford University; and Walter J. McNerney, Professor of Health Policy, Northwestern University.

Progress and Pessimism

by Dwight Lee

The only thing more persistent than progress is pessimism about further progress. Ever since the Industrial Revolution, we have experienced a widespread increase in material well-being, life expectancy, and leisure that literally could not have been imagined three centuries ago. Yet, this enormous progress is still accompanied by a steady stream of forecasts predicting impending crises and the end of progress.

Time magazine, for example, introduced its cover story on the "Endangered Earth" with a statement that mankind "may have no alternative to the bang of nuclear holocaust or the whimper of slow extinction." Senator Albert Gore, Jr., warns that "...we are being drawn toward the brink of ecological collapse." Brazil's Secretary of the Environment, Jose Antonio Lutzenberger, said "...the idea of sustainable growth is a contradiction in terms." And environmental activist Barry Commoner claims that "the ecosphere...is likely to end in global catastrophe."

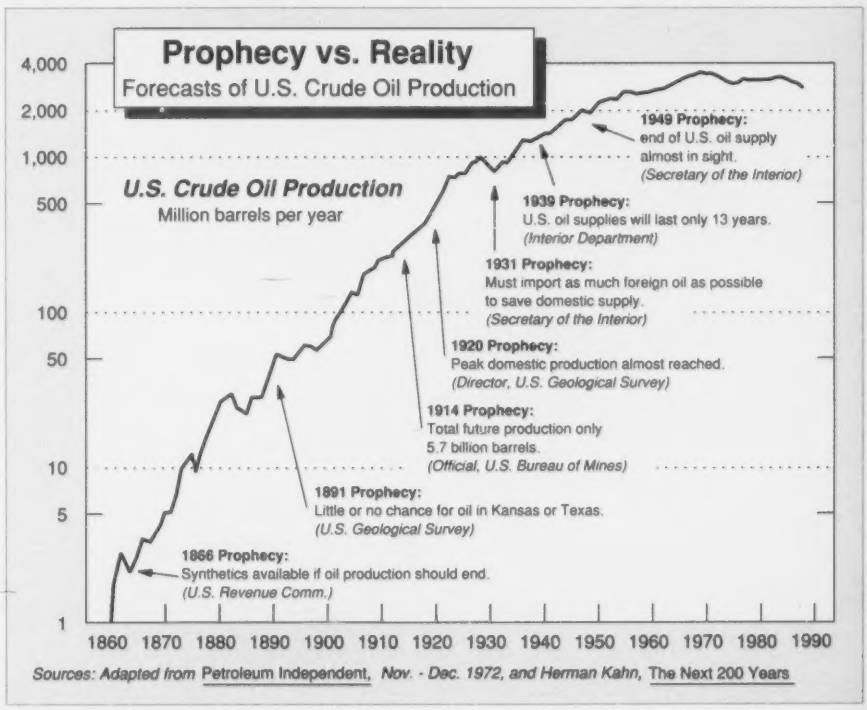
False Prophecies from the Past

Such pessimistic assessments of the prospects for progress are part of a long tradition of despair. One of the earlier, and best known, purveyors of gloom was Thomas Malthus, who in 1798 predicted that starvation and pestilence would limit the size of a population destined to a perpetual existence of bare subsistence. Another well-known English economist, William Stanley Jevons, wrote in 1865 that the exhaustion of coal supplies would soon bring industrial progress to a halt.

At the beginning of the present century, expert opinion was convinced that the supply of wood in the United States would soon be exhausted. As the *New York Times* headline put it: "Hickory Disappearing, Supply of Wood Nears End — Much Wasted and There's No Substitute" (October 31, 1908). And, as the chart shows, the experts have had us about to run out of oil almost from the time it began to be widely used.

Some of the most prestigious scientists in the past dismissed the possibility of innovations and advances in knowledge that today we take for granted. The British Royal Society responded to Thomas Edison's proposals by issuing the statement that Edison's ideas to electrify cities "defy scientific principle" and "wouldn't work." Lord Kelvin, President of the Royal Society, informed people in 1895 that "heavier-than-air flying machines are impossible." Charles H. Duell, who was the Director of the U.S. Patent Office, is quoted as saying in 1899 that "everything that can be invented, has been invented." Robert Millikan, a Nobel Prize winner in physics, stated in 1923 that "there is no likelihood man can ever tap the power of the atom."

Fortunately, creativity has never been respectful of expert opinion. Human progress is a history of the discovery of ingenious ways around, over, and through the obstacles that have stood in the way of our desire for greater material well-being. When man's natural creativity and persistent discontent are coupled with the incentives and information of the marketplace, we have a powerful correlation of forces pushing for progress.


Prophecy vs. Reality
Forecasts of U.S. Crude Oil Production
U.S. Crude Oil Production
Million barrels per year
4,000
2,000
1,000
500
100
50
10
5
1
1860 1870 1880 1890 1900 1910 1920 1930 1940 1950 1960 1970 1980 1990
1949 Prophecy: end of U.S. oil supply almost in sight. (Secretary of the Interior)
1939 Prophecy: U.S. oil supplies will last only 13 years. (Interior Department)
1931 Prophecy: Must import as much foreign oil as possible to save domestic supply. (Secretary of the Interior)
1920 Prophecy: Peak domestic production almost reached. (Director, U.S. Geological Survey)
1914 Prophecy: Total future production only 5.7 billion barrels. (Official, U.S. Bureau of Mines)
1891 Prophecy: Little or no chance for oil in Kansas or Texas. (U.S. Geological Survey)
1866 Prophecy: Synthetics available if oil production should end. (U.S. Revenue Comm.)
Sources: Adapted from Petroleum Independent, *Nov. - Dec. 1972, and Herman Kahn,* The Next 200 Years

Numerous examples of the expansion of the economy's useful resource base could be cited. Possibly the most obvious example in recent years is the computer. Consider the now almost prosaic use of computers to allow people to telecommute; to work with the same effectiveness at home as at the office. It has been estimated that if 12 to 14 percent of urban commuting is replaced by telecommuting, the annual reduction in U.S. petroleum consumption would come to 75 million barrels. Sand and knowledge combine to make the silicon chips that are the heart of computers which, in essence, become substitutes for petroleum.

While seldom recognized, and certainly underappreciated by those who are most vocal in their concern for our forests, chemicals are currently a major substitute for wood products. According to former Chairman of the Atomic Energy Commission, Dixy Lee Ray, "Through the use of wood preservatives in pressure-treated lumber for fences, porches, decks, and homes, we have saved a forest of trees two times the size of New England."

Other breakthroughs may expand the useful resource base beyond our current dreams. Recent advances in superconductors suggest the possibility of substituting ceramics for electricity production. With likely breakthroughs in nuclear fusion, sea water could become an inexhaustible source of energy by the next century.

Artificial Crises and Economic Progress

Despite the long history of market responses straight-arming one crisis after another, and the more recent history of government suppression of market responses perpetuating one crisis after another, the presumption is that a crisis calls for government solution. And if a real crisis is not available, an artificial crisis created by distortions and misinformation will serve just as well.

Consider the statements of some of those who hold themselves up as environmental experts. According to Richard Benedick of the U.S. State Department, while on assignment with the Conservation Foundation, "A global climate treaty must be implemented even if there is no scientific evidence to back the greenhouse effect." Stephen Schneider, a highly publicized environmental activist, states. "[W]e have to offer up scary scenarios, make simplified, dramatic statements, and make little mention of any doubts we may have. Each of us has to decide what the right balance is between being effective and being honest." Senator Timothy Wirth of Colorado has said, "We've got to ride the global warming issue. Even if the theory of global warming is wrong, we will be doing the right thing anyway, in terms of economic policy and environmental policy."

A brief look at some of the predictions of those who want to protect us against economic progress makes clear that indeed they are more interested in being effective (at creating artificial crises) than in being honest. One of the most absurd, but widely read and regarded, examples of the predicted end of progress is contained in the 1972 Club of Rome report, *The Limits to Growth*. They concluded that the only thing that could save civilization from collapse and ruin by the end of the twenty-first century was the immediate halt to economic progress.

At least the authors of *The Limits to Growth* were smart enough to make a prediction that extended beyond their lifetimes. Stanford biologist Paul Ehrlich cannot be accused of such a prudent approach. In the 1960s, Ehrlich informed us in his book, *The Population Bomb*, that sometime in the 1970s global famine would result in the starvation of hundreds of millions of people. As the end of the 1970s approached with per capita world food production increasing, Ehrlich decided it was time to adjust his prediction. The year 1985 was picked for the global famine. Not discouraged by the problem of timing, Ehrlich now proclaims that by the year 1999 over 90 percent of the U.S. population will perish because of famine and global warming. Ehrlich has been rewarded for his special prescience by being hired as a regular commentator for NBC television. There can be no doubt that many of the doomsayers have developed a vested interest in their predictions.

Conclusion

In the past, fears of a crisis were not likely to be widespread unless the crisis was real. Today, mass media and massive government can create crises out of little more than exaggerated rhetoric. In response to fears fomented and exploited by environmental extremists with media access, government action can, and often does, convert an artificial crisis into the real thing by mandating prohibitions, protections, and price controls that immobilize market responses.

Environmental extremism is, and will remain, a potential source of disruption. We should not give the extreme environmentalists credit for more power than they have, however, by succumbing to unfounded fears. Both history and economic analysis inform us that the forces propelling economic progress are powerful ones. In the absence of overreaching government responses to public fears, the combination of market incentives and human ingenuity create a momentum for progress that is too strong to be derailed by those whose primary energy comes from a naive longing for the end of progress.

Excerpted from *The Perpetual Assault on Progress*, May 1991, Center for the Study of American Business, Washington University in St. Louis. Dwight Lee is the Ramsey Professor of Economics at the University of Georgia and an adjunct fellow of the Center for the Study of American Business.

Immigration and Branch Rickey's Vision

by Julian L. Simon

Increasing the flow of immigrants presents the United States with an opportunity to realize many national goals with a single stroke. It is a safe and sure path — open to no other nation — to achieve all of these benefits:

- A sharply increased rate of technological advance, spurred by the addition of top scientific talent from all over the world.
- Satisfaction of business's demand for the labor that the baby-bust generation makes scarce.
- A lessening of the burden that retirees impose upon the ever-shrinking cohort of citizens of labor-force age, who must support the Social Security System.
- Rising tax revenues — resulting from the increase in the proportion of workers to retirees — that will provide the only painless way of shrinking and perhaps even eliminating the federal deficit.
- Improvement in our competitive position vis-à-vis Japan, Europe, and the rest of the world.
- A boost to our image abroad, stemming from immigrants' connections with their relatives back home, and from the remittances that they send back to them.
- Not least, the opportunity given to additional people to enjoy the blessings of life in the United States.

All the U.S. need do to achieve these benefits is further to relax its barriers against skilled immigrants. Talented and energetic people want to come here.

We tend to think of ourselves as a "nation of immigrants," but less than one out of fifteen people now in the U.S. was born abroad. The recent flow is less than a fourth as heavy as it was between 1901 and 1910. We are a nation not of immigrants, but rather of the descendants of immigrants.

Malthusian and Other Objections

Now let us consider the costs and benefits of immigration — even though economic issues may not be the real heart of the matter, often serving only as a smoke screen to conceal the true motives for opposition. The first objection — the "Malthusian objection" — is the idea that immigration dilutes the amount of capital per worker, which causes output per worker to fall. Nowadays, however, the most important capital is human capital — education and skills, which people own themselves and carry with them — rather than capitalist-supplied physical capital. Human capital is far more important in a country's development. And immigrants supply their own human capital.

Nowadays human capital — education and skills — is far more important than physical capital in a country's development. And immigrants supply their own human capital.

The second objection, the one that most captures the public's imagination, is welfare payments. In an analysis of Census Bureau data I found that, aside from Social Security and Medicare, about as much money is spent on welfare services and schooling for immigrant families as for citizens. When programs for the elderly are included, immigrant families receive far **less** in public services than natives. And U.S. immigrants pay much more in taxes than they receive in benefits.

Some cities and states with disproportionately high immigration do incur significant costs and complications when immigrants first arrive. Perhaps the cities should get more federal assistance. The taxes paid by the immigrants to the federal government will later more than offset this transfer to the cities.

The third and most dramatic argument against immigration has been that foreigners take jobs held by natives and thereby increase native unemployment. In the shortest run, additional immigrants in a given occupation must to some degree lower wages and/or increase unemployment in that occupation. But because immigrants come with a variety of skills, workers in most occupations feel little impact.

A good-sized body of competent recent research shows that immigration does not exacerbate unemployment, even among directly competing groups. The explanation is that immigrants not only take jobs, but also create them. Their purchases increase the demand for labor, leading to new hires roughly equal in number to the immigrant workers. Immigrants also create jobs directly by opening new small businesses — which are the main generator of new jobs in the economy — in larger proportion than do natives.

(continued on p. 7)

Ellis Island, Historic Gateway for U.S. Immigrants.

Illustration by T. O'Brien Slater.

Boosting Productivity

Most important in the long run is the boost that immigrants give to productivity. Some of the productivity increase comes from immigrants working in industries and laboratories that are at the forefront of world technology. Remember that the development of the atomic bomb hinged on the participation of such immigrants as Enrico Fermi, John von Neumann, and Stan Ulam. Contemporary newspaper stories continue this historical saga, noting the disproportionate numbers of Vietnamese and other Asian immigrant youths who achieve distinction in competitions such as the Westinghouse Science Talent Search. Ben Wattenberg and Karl Zinsmeister of the American Enterprise Institute write that among the 40 1988 finalists, "22 were foreign-born or children of foreign-born parents from Taiwan, China, Korea, India, Guyana, Poland, Trinidad, Canada, Peru, Iran, Vietnam and Honduras."

The Real Reasons for Opposition

There are various reasons for our failure to take in more immigrants, despite the clear-cut benefits of doing so. The first is ignorance of the benefits described above. Second is the opposition by special interests, such as organized labor (which wants to restrict competition for jobs) and ethnic groups (whose members often fear that immigration will cause their proportion of the population to decrease). The third reason is well-organized opposition to immigration and total lack of organized support for it.

Another check to immigration is nativism or racism, a motive that often lies beneath the surface of the opposition's arguments.

The fourth check to immigration is nativism or racism, a motive that often lies beneath the surface of the opposition's arguments. Rita Simon of American University who has studied the history of public opinion toward immigrants has found that the arguments against immigration have remained eerily identical.

In the first half of the nineteenth century Irish immigrants in New York and Boston were seen as the unassimilable possessors of all bad qualities. The 1884 platform of the Democratic party stated its opposition to the "importation of foreign labor or the admission of servile races unfitted by habit, training, religion or kindred for absorption into the great body of our people or for the citizenship which our laws confer." In the 1920s the *Saturday Evening Post* also directed fear and hatred at the "new immigrants" from Southern and Eastern Europe: "More than a third of them cannot read and write; generally speaking they have been very difficult to assimilate."

Today many people still privately sympathize with such views.

Political Advantages

Political power and economic well-being are intimately related: a nation's international standing is heavily influenced by its economic situation. And today the future of any country depends entirely on its progress in knowledge, skill and productivity. That's why immigration safely, cheaply, and surely provides the U.S. with perhaps the greatest opportunity that a country has ever had to surpass its political rivals.

Immigration policy presents the U.S. with an opportunity like the one that faced the Brooklyn Dodgers in 1947, before blacks played baseball on any major-league team. Signing Jackie Robinson and then Roy Campanella, at the price of antagonizing some players and club owners, put the Dodgers way ahead of the pack. In the case of immigration, unlike baseball, no other "team" can duplicate our feat, because immigrants mainly want to come here. All we need are the vision, guts, and ambition of Dodger general manager Branch Rickey.

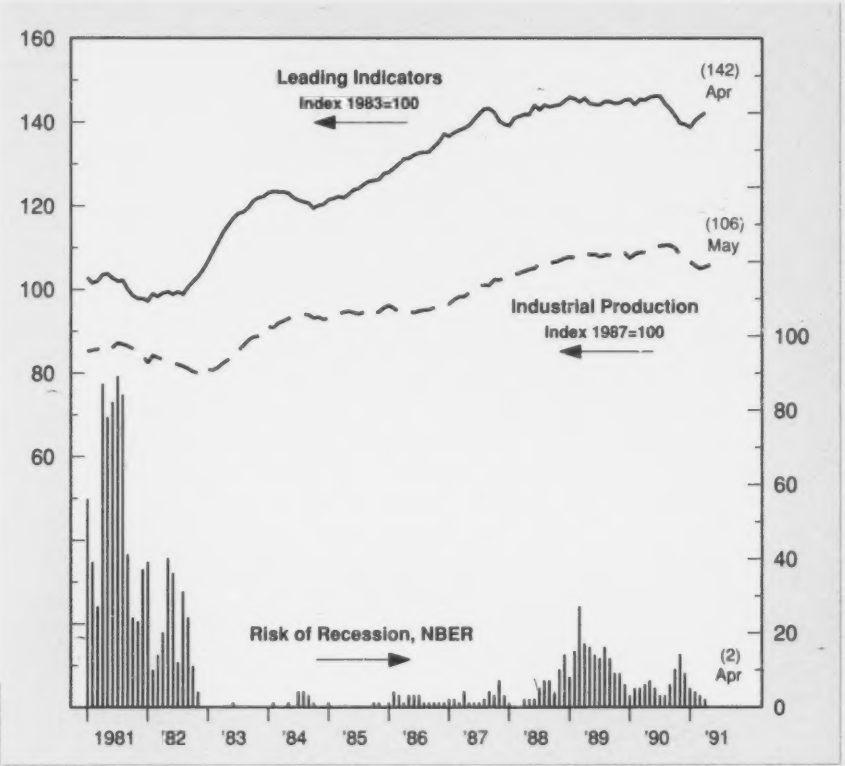
Excerpted from "The Case for Greatly Increased Immigration," *The Public Interest*, Winter 1991. Julian L. Simon is Professor of Business Administration at the University of Maryland, and the author of *The Economic Consequences of Immigration* and, most recently, *Population Matters: People, Resources, Environment and Immigration.*

Conference Board Stat File

Robust U.S. Competitive Position

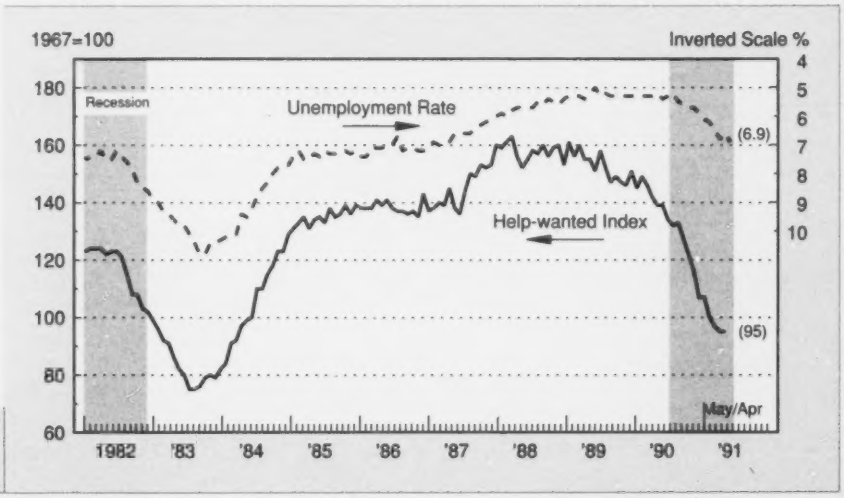
The new data in our Stat File this month strongly affirm that the cyclical upturn is now behind us, but do not otherwise enlighten us meaningfully about the economy. We've added one new chart (p.10, bottom) courtesy of Morgan Stanley Economic Research. This chart provides an alternative way of showing how favorably or unfavorably a country's competitive position has been treated by the international currency markets. What these data show is how difficult it is at present for foreign manufacturers to compete against American producers. The dollar has been so low, in fact, that on average foreigners are incurring losses on imports to the United States. As Robert Gay of Morgan Stanley put it, "...U.S. producers should be able to maintain or even to increase their share of the world's production of tradable goods." *(Note: data for Conference Board series in this section are available upon request from Ken Goldstein at 212-339-0331.)*

Early Warning Indicators



Change in cyclical direction seems almost assured.

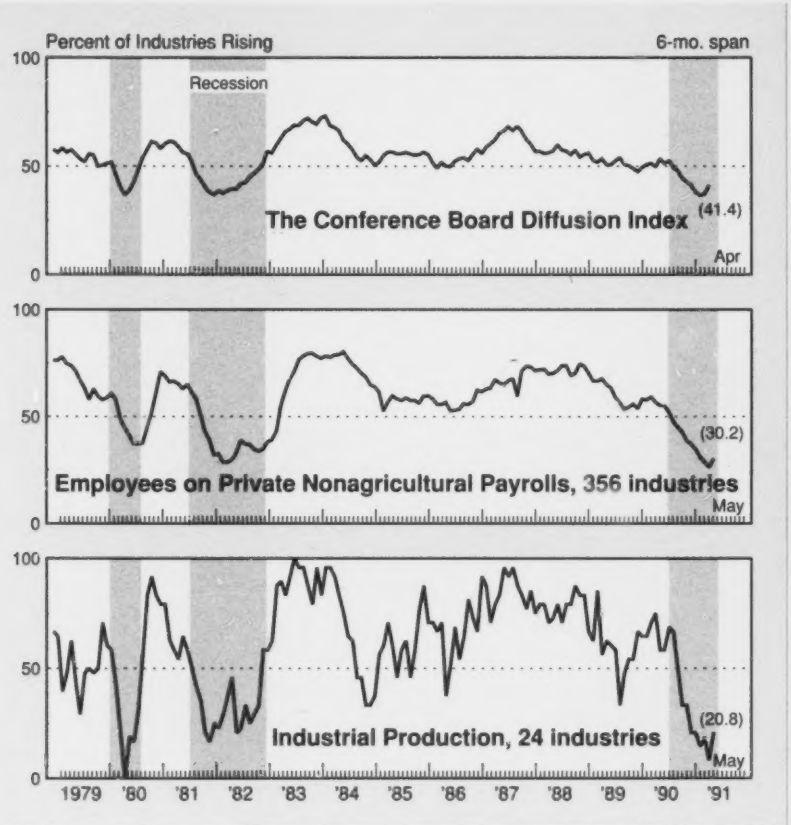
Help-wanted Advertising and Unemployment



As usual, labor market indicators slow to turn at the end of recession.

Conference Board Stat File

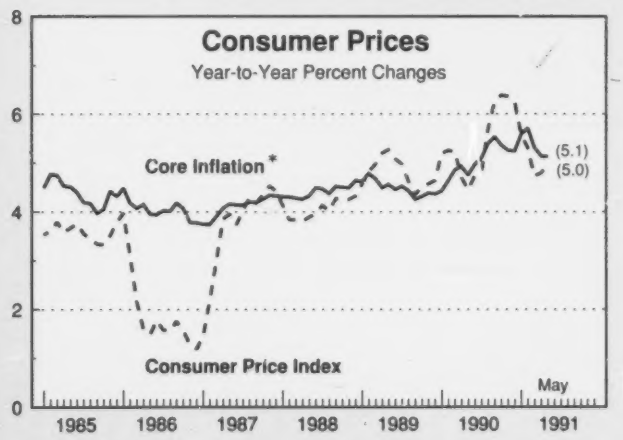
Indexes of Economic Momentum



All three indexes show the beginning of a turn in momentum.

Core inflation rates still seem slow to subside.

Inflation Fundamentals

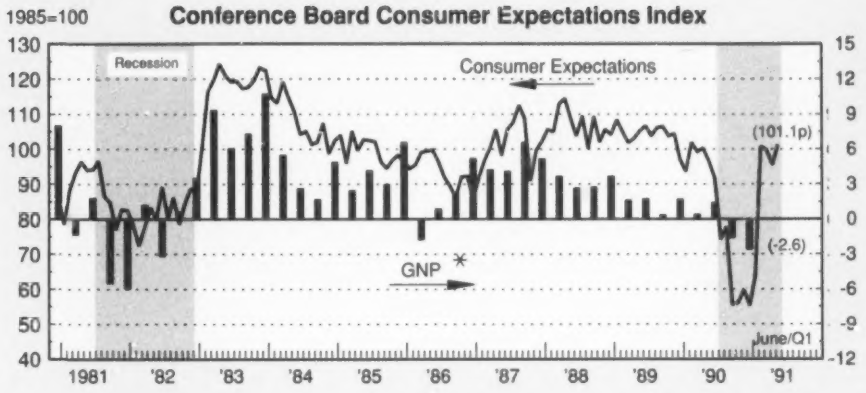


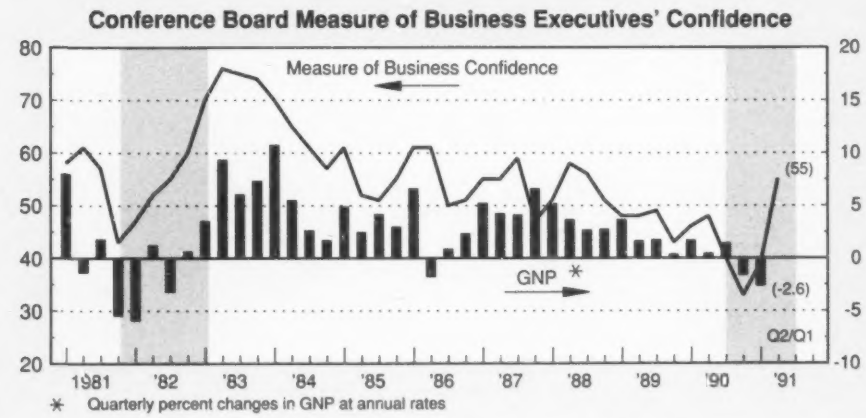
* Core Inflation = CPI excluding food at home and energy.

* Core employment-cost inflation = wages and salaries of private sector workers excluding sales personnel (i.e., excluding the benefits that are part of the ECI).

Conference Board Stat File

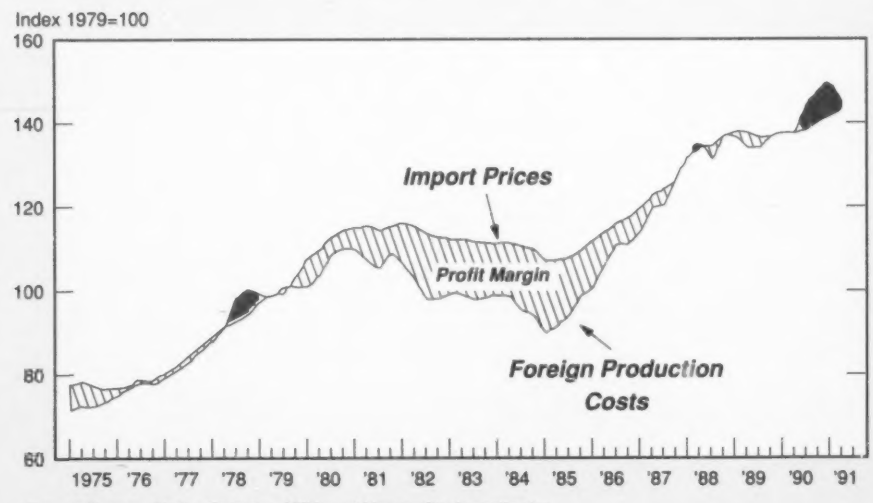
Confidence





No signals here of reluctant attitudes.

Import Prices and Profit Margins



Imports into the U.S. currently reap losses, not profits.

Inside the Crystal Ball

		UCLA	MERRILL L.	DU PONT	GEORGIA ST.	NORTHERN TRUST	CONF. BOARD	EATON	L.H. MEYER	DRI	WEFA	MICHIGAN – RSQE		
Date of Forecast		June	June	June	June	June	June	June	June	June	June	June		
Gross National Product		(Quarter-to-quarter percent change, constant dollars, seasonally adjusted at annual rates)												
		%	%	%	%	%	%	%	%	%	%	%		
Actual	1990 4Q	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	4Q 1990	Actual
	1991 1Q	-2.8	-2.6	-2.6	-2.6	-2.6	-2.6	-2.6	-2.6	-2.6	-2.6	-2.6	1Q 1991	
Forecast	2Q	-0.6	-0.4	-0.6	0.2	1.0	2.4	1.4	-0.4	0.5	0.9	0.6	2Q	Forecast
	3Q	1.9	0.9	2.2	3.0	3.3	2.3	5.4	1.8	3.0	2.5	2.7	3Q	
	4Q	3.6	4.6	3.0	3.2	3.3	1.6	4.1	2.8	3.2	3.5	3.3	4Q	
	1992 1Q	4.7	4.5	3.2	3.1	3.1	2.4	3.3	3.9	3.7	4.2	2.6	1Q 1992	
	2Q	4.4	3.1	3.7	1.5	3.4	1.8	2.0	3.4	3.2	4.4	2.2	2Q	
	3Q	3.6	2.5	3.9	2.7	3.3	2.2	2.0	3.4	2.3	3.9	2.6	3Q	
	4Q	2.1	2.1	3.8	2.2	3.1	2.5	2.1	2.6	1.8	3.1	2.3	4Q	
	1993 1Q	2.0		3.7			2.4	4.0	3.3	2.4	3.0		1Q 1993	
	2Q	1.6		3.8			2.2	3.5	2.9	2.8	2.5		2Q	
Inflation (GNP Deflator)												(Percent change from same quarter one year earlier)		
Actual	1990 4Q	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	1990 4Q	Actual
Forecast	1991 4Q	3.1	4.4	4.1	3.8	4.3	4.5	3.0	4.0	3.5	2.8	3.9	1991 4Q	Forecast
	1992 4Q	2.9	4.1	3.6	3.5	3.9	4.7	2.6	2.9	3.1	3.3	3.6	1992 4Q	
30-Yr Treasury Bond Rate														
Actual	1990 4Q	8.6	8.6	8.6	8.6	8.6	8.6	8.6	8.6	8.6	8.6	8.6	4Q 1990	Acutal
	1991 1Q	8.2	8.2	8.2	8.2	8.2	8.2	8.2	8.2	8.2	8.2	8.2	1Q 1991	
Forecast	2Q	8.4	8.3	8.3	8.3	8.3	8.1	8.3	8.2	8.3	8.2	8.3	2Q	Forecast
	3Q	8.5	8.4	8.2	8.4	8.4	8.3	8.7	8.0	8.4	8.3	8.3	3Q	
	4Q	8.6	8.5	7.8	8.4	8.2	8.3	8.6	7.9	8.7	8.5	8.2	4Q	
	1992 1Q	8.7	8.7	7.7	8.5	8.3	8.6	8.6	8.0	8.8	8.6	8.1	1Q 1992	
	2Q	8.7	8.6	7.8	8.7	8.3	8.6	8.6	8.2	8.8	8.7	8.1	2Q	
	3Q	8.8	8.6	7.9	8.7	8.4	8.6	8.7	8.2	8.6	8.8	8.0	3Q	
	4Q	8.9	8.5	7.9	8.6	8.5	8.6	8.7	8.2	8.4	8.9	7.9	4Q	
	1993 1Q	8.9		8.0		8.6	9.1	8.8	8.1	8.4	9.0		1Q 1993	
	2Q	8.9		8.0			9.1	8.6	8.0	8.3	9.1		2Q	
Unemployment Rate												(Percent, quarterly)		
Actual	1990 1Q	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	1Q 1990	Actual
Forecast	1991 4Q	6.5	6.9	6.7	6.9	6.9	6.9	6.8	6.9	6.9	6.7	6.7	4Q 1991	Forecast
	1992 4Q	5.8	6.5	6.3	6.7	6.5	6.6	6.7	6.3	6.4	6.1	6.5	4Q 1992	
	1993 2Q	5.8		6.1			6.4	6.2	6.0	6.3	6.0		2Q 1993	

The Conference Board
845 Third Avenue
New York, N.Y. 10022

Second Class
Postage paid at New York, NY
and at
additional mailing offices

Acquisitions
Statistical Reference Index
4520 East West Highway, Suite 800
Bethesda, MD 20814

Industry Outlook Report

July/August 1991

Overview

Edgar R. Fiedler
The Conference Board

The industry specialists we have collected to report on the outlook for the next year or two are agreed that happier days are ahead, at least in the sense that the business cycle is turning toward expansion again. They are not quite agreed, however, on the timing of that event: Some say the turn has already taken place, but others look for it during the second half of the year.

The degree of optimism is also a mixed bag, clearly on the cheerful side of the spectrum, but generally restrained. On average, this group is more hopeful than our panel of last April.

The closest thing to ebullience is found in the report on capital equipment, where Mitch Quain says that overall the sector is "healthier than at any time in the past ten years. Costs are down, companies are lean, ... and all parts of the world are moving capacity to the United States."

More representative of the panel's tone is Roz Wells' comment about retailing, "This time, the usual bounceback will be muted by a less than robust recovery in housing and moderate gains in income." Similarly, Maryann Keller suggests the "cyclical recovery in vehicle sales is likely to be shallower than in the past because the purchase price of new cars has risen faster than incomes...Almost 25 weeks of household income are needed to buy the average car today compared to 19 weeks in 1980."

Randy Jayne probably identified the consensual position of the group when he spoke of the *bittersweet* outlook for aerospace. He contrasts "the continuing reductions in defense spending" against the encouraging future for commercial transport, and points to the "consolidation, shakeout, dropouts, and creative partnering" that will create "a smaller set of leaner companies" in the industry.

The report can be summarized by noting that the recession is over, or nearly so, and sooner or later the recovery will lead most industries back to better times.

Motor Vehicles

Maryann N. Keller
Furman Selz

During the second half of 1991 vehicle demand should gradually improve from the extremely depressed sales rates of the first half. Nevertheless, total vehicle demand will only reach 12.7 million units for the year, the worst since the 1982 recession when 10.6 million cars and trucks were purchased. Peak demand occurred in 1986, when total sales reached 16.4 million.

Because of growth in Japanese "transplant" production, General Motors, Ford and Chrysler will assemble only 4.2 million cars in 1991, 1.1 million more than in 1982, but down 3.2 million since 1986 when these three companies produced 7.4 million cars. Although Japanese auto imports have fallen, local assembly increased supply and raised the foreign brand share of the market to 35.5 percent in 1991, compared to 27 percent in 1982. Honda and Toyota each sell more cars than Chrysler, which has been pushed into fifth place.

The battle for market share intensified with aggressive sales by rental companies of "nearly new" four-months-old, low-mileage rental cars, retailed at substantial discounts to the prices of brand new models. Almost two million such cars were bought in 1991 and they reduced new-car sales to private customers. Automakers have modified the programs for 1992 so that fewer of the "nearly new" cars will be sold to the public.

Although domestic companies reduced costs, competition reduced profitability, so that all three will report losses of more than $3 billion for the year. Competition has forced the domestic companies to continue high levels of capital spending in spite of the losses. GM and Ford both have sufficient access to capital but Chrysler has been forced to sell assets to fund product investment. Competitive advantage has shifted to those with sufficient capital at affordable rates.

The cyclical recovery in vehicle sales is likely to be shallower than in the past because new car prices have risen faster than incomes. Today's new car costs $16,500 compared to $7,574 in 1980. Almost 25 weeks of household income are needed to buy the average car today compared to 19 weeks in 1980. A decade ago the industry lengthened maturities of auto loans to 60 months. Since loan maturities will not be extended further, industry price hikes above increases in income will reduce vehicle demand or shift the mix in favor of less expensive models.

Currently consumers are being treated to heavily subsidized leases. These cannot be continued, however, because they are based on inflated residual values.

Next year auto sales could rise to 9.5 million units and trucks to 4.6 million units, an increase in total vehicle demand of 1.4 million units over 1991.

Aerospace

E. Randolph Jayne
McDonnell Douglas
Missile Systems Co.

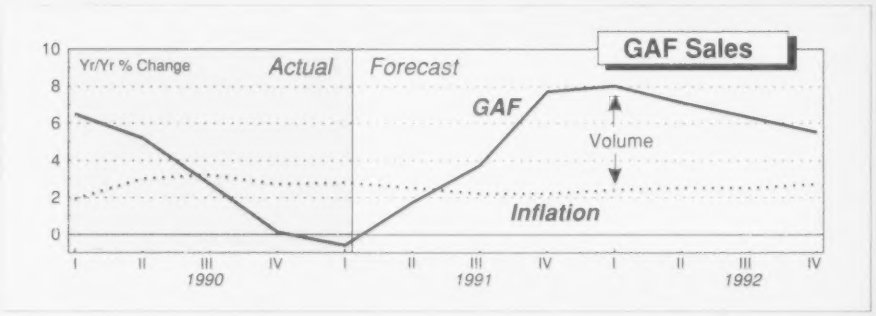
The ten year outlook for aerospace is indeed bittersweet. On the one hand, the continuing reductions in defense spending here and abroad portend downsizing, consolidation, and at some point, fewer total weapons producers. In space, the Space Station and other initiatives hold the possibility of sustaining a portion of the current industry through the decade, but budget constraints threaten here too.

The good news, and the encouraging future, lies in commercial transport. World airline capacity growth, plus normal replacement of older inventory, suggests continued strong demand in this sector well into the twenty-first century. Revenue passenger miles will more than triple by 2010, according to industry forecasters. Existing 1991 airliner backlog stands at over 3500 planes, valued at $200 billion.

Taken together, these military, space, and commercial forecasts suggests two trends for the decade of the '90's. First, companies will strive to shift resources from defense to commercial aerospace, a process far easier for airframe, electronics, and component makers than for producers of land and sea weapons. Second, consolidation, shakeout, dropouts, and creative partnering will characterize all of aerospace, as a smaller set of leaner companies compete for a smaller defense market and a growing commercial aircraft business. For those companies able to straddle and, when necessary, shift back and forth between those markets, the future will be bright. Others, less able to restructure and transition, will join the slow but steady casualty list of world aerospace since World War II.

General Merchandise Retailing

Rosalind Wells
Wells & Associates



After two very tough Christmas seasons, general merchandise retailers finally have something to look forward to. The economic evidence clearly is pointing to a second half turnaround. GAF sales (sales at general merchandise stores, apparel specialty stores and furniture and homefurnishings stores) have already bottomed out in April and May. No doubt, some of the strength in May was due to warmer-than-usual weather that prompted the purchase of summer clothing, outdoor furniture and cooling equipment. Although some of these sales may have been accelerated, consumer demand is responding to the better economy and will continue to improve into next year.

This year's quarterly sales pattern will be the opposite of last year when increases deteriorated as the year progressed. The economic recovery and easy comparisons to holiday 1990 will produce hefty GAF sales gains of close to 8 percent for retailers in the fourth quarter of 1991. Yearly results, however, will average 3 1/2 percent — hardly better than last year. Next year, as the economy continues to expand, GAF sales will be up about 6 1/2 percent. Consumers will remain very price conscious over this period, thereby preventing an upsurge in GAF prices. Sales volume advances will, therefore, improve from 1 percent in 1991 to 4 percent in 1992.

During recovery, periods durables such as major appliances, which have been cut back the most, normally show the strongest rebound. This time, the usual bounceback will be muted by a less than robust recovery in housing and moderate gains in income. Instead, decorative home textiles including bed and bath items will outperform the higher ticket purchases. Apparel and accessories will do well — especially if prices are kept under control — with women's and children's experiencing higher growth than men's. Sales of leisure goods, including home electronics, sporting goods, toys, hobbies and photography have suffered due to cutbacks in discretionary spending during the recession. Sales of this merchandise will get a lift as consumers have more money to spend to fulfill pent-up demands.

Financial Services

Francis H. Schott
Consultant

The financial services industry should benefit substantially from the likely end of the recession in the second half of 1991 as well as from the subsequent expansion in 1992. This outlook is a welcome change from the seriously depressed profit and employment conditions of the past three years.

Naturally, the outlook differs widely among the various segments of the industry. Mutual funds have been successful in attracting new funds and investors in a growing variety of products — specialized equity, bond and money market funds. Therefore, the asset-management segment of the industry has been doing well and should continue to do so.

The investment banking and brokerage community is the sector of finance likely to benefit most from the impending recovery. Stock and bond offerings were rising in the first half of 1991 and should mount further. Trading volume is running 10-20 percent above year-ago figures, and profits should register similar increases over the next 18 months.

Within the insurance industry, the property/casualty segment does best in a low-inflation, early-recovery environment and thus enjoys a good outlook. The life, pension and health companies continue to experience ferocious competition, cost pressures and asset problems. Their recovery will be slow.

The depository institutions have been the most recession-affected sector of finance. Their asset problems, concentrated in commercial real estate, will be bothersome until mid-decade. The savings & loan shakeout may be at the point where the survivors will do better from now on, as residential real estate revives. However, the full extent of the commercial banks' real estate and HLT (highly leveraged transactions) problems is only now becoming apparent. The bank's profit outlook remains dubious except for selected regionals and locals. The entire industry faces consolidation and internationalization moves during the 1990s. By decades' end many foreign-institution names will become household words here. There is also a good chance that top U.S. institutions will be successful in the (consolidated) European market and in the Japanese market.

Telecommunications

John S. Bain
Raymond James & Associates

After an almost hysterical runup in 1989, stocks of the telecommunications common carriers have underperformed the general market indexes. The cause of this relative lack of performance can be traced to overoptimism regarding the industry and a naive belief among investors that the telecommunications industry was somehow "recession proof." The optimism related to the prospects for cellular mobile radiotelecommunications service, to the supposed benefits of "reregulation," and to the notion that the common carriers had somehow become "growth" companies. In addition, it was widely believed that the fundamental growth in the demand for telecommunications service had reached a permanently high rate in the mid-double digits.

All of these notions have been to some extent discredited. The demand for service has proven to be sensitive to both the economy, and to the price reductions that characterized the industry from 1984 through 1989. At present, it appears that such price reductions are at an end, with the result that most observers now feel that long-term growth in the range of 8 percent to 10 percent is more likely. Even such sure-fire, "can't miss" investment ideas as cellular have suffered a significant decline in market valuations since the late-1989 peak.

However, although the positives may have been exaggerated, there is some truth to all of them. Cellular is a growing and valuable technology. Price cap and other alternative forms of regulation do offer potential benefits to investors. And the telecommunications industry is somewhat recession-resistant, although less than was commonly thought.

The 1992 Outlook. Assuming that we really are near the bottom of the recession, resumption of economic growth should bring a sharp rebound in the growth of demand. In particular, access-line growth should return to the 3.5 to 4.5 percent rate that characterized most companies until 1990. On the long-distance side, we anticipate a rebound to 10 percent or better in 1991, up from 7 percent or so in 1991, with long-term demand growth settling out in the 8 to 10 percent range.

If the market has been surprised by the extent to which the recession has affected the industry on the downside, then it should be equally surprised by the extent of the rebound. We estimate that revenue growth will nearly equal volume growth for the first time since 1984. What this adds up to is a healthy outlook for both volume and revenue growth in the latter half of 1991 and into 1992.

Airlines

Helane Becker
Lehman Brothers

The airline industry is on the road to recovery. After nearly two years in recession, in which earnings have deteriorated dramatically, we expect gains this summer to continue into 1992. Since mid-1989, airline traffic growth stalled, while earnings sequentially declined, until the industry reported $5.2 billion worth of losses in the August 1990-March 1991 period.

Beginning towards the end of March, and then continuing through 1991's second quarter, airline traffic growth began to recover. Much of this recovery is directly attributed to promotional fare activity. The industry reinstituted Kids Fly For Half Price, which prompted many families to book summer vacations. Other discount fares involve travel to and from Europe, and in some cases include doubled or triple mileage for frequent fliers.

As the U.S. economy recovers, the airline industry's recovery will accelerate. This cycle was a particularly difficult one for a number of airlines, especially as there are a record three operating in bankruptcy. Consumers have been actively voting for their favorite airline. Market share in the airlines considered to be financially solvent is increasing, while that of other, weaker airlines is decreasing.

Part of the reason for the decline in market share among those airlines considered poor credits is what we refer to as the transfer of wealth. Wealthy airlines have been buying up the assets of their financially weak counterparts. The financially weak airlines gain cash to continue funding operations while they attempt to restructure. Unfortunately, these airlines tend to engage in payroll pricing, and they keep yields low. This has a negative effect on all other airlines.

Over the next few quarters, we expect the industry to report better operating results. The cost of jet fuel is down dramatically. Traffic is beginning to resume its growth. Pricing is likely to improve later in 1991, as airlines eliminate a lot of the incentive programs for travelers. If traffic growth picks up, pricing improvements are likely to follow.

Airline Operating Results ($ mil)

	1H91E	2H91E	1992E
Revenues	$24,456	$31,000	$63,400
Expenses	26,343	30,000	61,900
Operating Income	(1,887)	1,000	1,400
Net Income	(2,200)	650	975

Clearly, we are looking for a better second half of 1991 than we had in the first half, as well as a 1992 that will be significantly better than 1990 or 1991.

Capital Equipment

Mitchell Quain
Wertheim
Schroeder & Co.

"Cusping" — that's where the domestic capital-goods industry is today. Suppliers of capital equipment experienced a sharp and sudden decline in demand beginning with the invasion of Kuwait last August, culminating in the first quarter of 1991. Ironically, the effect was most severe in those sectors of capital equipment that are normally the most stable. That is, providers of maintenance supplies, spare parts, and companies that sell product through distribution experienced the most severe declines at the manufacturing level. Though the manufacturers — since they've tended to adopt "just-in-time" supply practices — were inventory lean, their distributors and users naturally liquidated inventory. The domestic industry today has ended that liquidation.

The sectors of capital equipment most closely tied to industrial production have already seen some recovery. Heavy-duty truck orders in April and May rebounded above 125,000 units, compared to a trough of 70,000-80,000 in the first quarter of 1991. A similar rebound occurred in the truck trailer industry. Recovery has not yet surfaced for the normally stable fluid power industry — the hydraulics, cylinders and valves used to power industrial equipment — but that seems to be due to the inventory cycle at the distribution level. The correlation with industrial production should naturally result in a recovery in the second half of this year. Similarly, the industrial lift-truck industry, long thought to be cannibalized by automated material handling systems, is likely to experience its normal cyclical rebound later this year. Finally, suppliers to the early-cycle housing and automotive industries, are looked upon favorably, likely to fully participate in this rebound.

Overall, the U.S. capital equipment sector is healthier than at any time in the past ten years. Costs are down, companies are lean, the rate of growth of productivity rivals virtually any part of the world, and companies located in all parts of the world are moving capacity to the United States. A more favorable federal tax structure relative to other countries is a recent positive. Higher exports have been a result, with the merchandise trade deficit nearly disappearing.